

## Consultation on Proactive Work

Comments should be sent to [commentletters@efrag.org](mailto:commentletters@efrag.org) by 30 September 2010

### 1. Introduction

1.1 An important part of EFRAG's activities is to undertake proactive work to anticipate issues and signal ways to improve financial reporting in Europe. 'Proactive' in this context is about providing thought leadership and promoting debates on critical financial reporting issues in Europe. This is principally achieved through influencing the work of the IASB. Earlier this month EFRAG released its Strategy for its Proactive Activities *Focus on Improvement* which can be found on our website at [www.efrag.org](http://www.efrag.org). One of our strategic aims is to ensure that our proactive work leads to practical solutions to relevant financial reporting issues. It is, therefore, key that the work we do responds to the needs of European constituents. Accordingly, our efforts need to be targeted at the most important issues, offer thoughtful and well-researched analyses of the issues and promoting workable solutions. Our resources are limited so we need to ensure we deploy them wisely to have the greatest impact in serving our European constituents.

1.2 As our role is to listen and respond to our constituents, we would like your assistance in helping us to:

- ***identify the areas where you think we should undertake proactive work***; and
- ***prioritise those areas of interest***.

1.3 We appreciate that there are many calls on your time at present with all the significant changes being proposed to IFRS so we have tried to keep our questions brief and focused. However, please feel free to add additional comments which you think would be helpful in improving our understanding of the issues that are most important to you, particularly, where they are likely to make a demonstrable improvement to financial reporting in Europe.

### 2. How we will consider your input

2.1 EFRAG will carefully consider the comments provided. We will identify common themes and issues and use it as a key input to shape our proactive work going forward.

Your input will also be useful to inform our discussions with the IASB about their priorities post-2011.

Our intention is to publish a feedback statement in October setting out what you have told us and how we will propose to respond to the main issues and suggestions made. It is important to us to ensure that our decision-making is open and transparent and fairly reflects the views of our constituents.

### **3. How we influence the IASB**

3.1 To be a strong European voice in a global environment continues to be significant challenge for EFRAG. Whilst we are told that our comment letters are widely read and are influential in the standard-setting process we recognise the need to influence that process early and also to provide thought leadership across Europe on financial reporting matters. There are several ways we think we can make a contribution to improving financial reporting in Europe. In particular, EFRAG is of the view that it is important to undertake early-stage proactive work – that is, to identify issues and develop proposals well ahead of them being added to IASB’s active work programme.

3.2 Proactive work can take several forms but with an emphasis on developing work at an early stage in the process, it is likely that our emphasis will be on developing the accounting model (concepts and principles) that underpins IFRS or undertaking in-depth analysis of specific financial reporting issues. It may also be worthwhile to undertake, as we have done in the past, short-term projects that address a particular aspect of proposals under development by the IASB, for instance the work we did on the Expected Loss Model to support debate in Europe about an appropriate impairment model for financial instruments.

3.3 Whilst not driven by the active work programme of the IASB, EFRAG believes that it is important that its proactive work complements the current development of IFRS. That is, to be relevant our proactive work should not be restricted to developing cutting-edge proposals for changes in the accounting model but should also aim to address real and important issues encountered in practice within the European environment. It is also relevant to note that we expect our work to complement that of other bodies (such as CESR) that also have an interest in improving financial reporting in Europe.

3.4 EFRAG is committed to work with National Standard-Setters across Europe, particularly those that pool resources through the EFRAG Planning and Resources Committee (EFRAG PRC). That model of working promotes collaborative projects and the efficient use of resources.

3.5 We may also work with other partners on proactive projects where we have a common interest in addressing a financial reporting issue. Our way of working on proactive projects is driven by what we think will achieve the best possible outcome.

#### 4. Current Proactive Projects

4.1 EFRAG has undertaken proactive projects over the years on a range of topics such as performance reporting, accounting for pensions and revenue recognition. Table 1 ‘Current Proactive Projects’ below sets out our active projects. Project status and developments are published in EFRAG PRC Summaries available at [www.efrag.org](http://www.efrag.org).

**Table 1: Current Proactive Projects**

<b>Project*</b>	<b>Project Description</b>
<b>Corporate Income Tax</b> (ASB/EFRAG/GASB)	The aim of the project is to critically examine key aspects of accounting for corporate income tax separately from the requirements in existing IAS 12, with a view to develop a Discussion Paper that starts from first principles and sets out proposals that may form the basis of a new standard on accounting for corporate income taxes.
<b>Business Combinations Under Common Control (BCUCC)</b> (ANC/EFRAG/OIC )	The project aims to identify, analyse and discuss the financial reporting practices used in the major markets to account for BCUCC and similar transactions in consolidated and separate financial statements.  The intention is to propose a conceptual model to consider and evaluate the different accounting treatments for BCUCC.
<b>Disclosure Framework</b> (ANC /ASB/EFRAG)	The aim of this project is to move beyond describing the problem of a lack of coherence and clutter in the financial statements to proposing a solution or model for the presentation and display of information in the notes to the financial statements.
<b>Effects Studies</b> (ASB/EFRAG)	The main objective of the project is to develop proposals for a framework by which the effects of accounting standards can be considered by standard-setters, notably the IASB, in developing new standards and major amendments to existing standards. Standard-setters have for many years wrestled with ways in which they can determine the effect of accounting standards. To date such analyses have been restricted to a qualitative assessment of costs and benefits.  In terms of content, the aim is to set out some principles and proposals for considering the effects of accounting standards, and how they might be embedded and articulated at each stage of the standard-setting due process.
<b>Business Model</b> (ANC/ASB/EFRAG)	This project aims to explore the relationship between an entity’s business model and financial reporting.

\* National Standard-Setters engaged in EFRAG Proactive projects: Autorité des Normes Comptables (ANC); UK Accounting Standards Board (ASB), German Accounting Standards Board (GASB) and Organismo Italiano di Contabilità (OIC).

## 5. Possible Proactive Projects

5.1 Maintaining high quality in our proactive work remains a key goal. Accordingly, it is important that we prioritise our proactive work to make sure we make the best use of our limited resources. Our priorities must be guided by identifying those areas where we are likely to have the greatest impact.

### Questions to Constituents

1. Prior to this consultation were you aware of EFRAG's Proactive Accounting in Europe (PAAinE) publications? (Copies of publications can be found at <http://www.efrag.org/content/default.asp?id=4109>) Did you find them useful and why or why not? In what ways do you think they could have been improved? Do you think they had a sufficient focus on European issues?
2. Based on the description above (under 'How we influence the IASB'), at what point in the standard-setting process should EFRAG focus its proactive work? Also are there specific aspects of financial reporting where we should concentrate our activities?
3. Table 2 'Proposed Proactive Projects' below identifies projects where EFRAG considers it may be useful to undertake proactive work. Can you rank the projects from most to least important based on EFRAG's strategic aims:

#### Proactive Strategic Aims

Aim 1: Influence the development of global financial reporting standards;

Aim 2: Engage with European constituents to ensure we understand their issues and how financial reporting affects them;

Aim 3: Provide thought leadership in developing the principles and practices that underpin financial reporting; and

Aim 4: Promote solutions that improve the quality of information, are practical, and enhance transparency and accountability.

4. If there are other projects you consider more important include them in your ranking and provide a short description of them along with your reasons as to why you believe they are important for EFRAG to consider.

**Table 2: Proposed Proactive Projects**

Rank	Project	Description
	European perspective on development of post implementation reviews (Post-implementation review policy)	The IASB has signalled that post-2011 it will devote a significant amount of its efforts assessing the effectiveness of extant IFRS. It is therefore important for European constituents to set out what the objectives of post-implementation reviews should be, how they should be conducted, what due process the IASB should follow and how the results from such studies should flow back into the standard-setting process. Accordingly, this project would be aimed at developing a policy (including a methodology) articulating the European view on how post-implementation reviews should be undertaken.
	Develop European Input to the IASB's post-implementation review of IFRS 3 'Business Combinations'*	The IASB has suggested that it will undertake a post-implementation review of IFRS 3 'Business Combinations'. It will be important that the European experience of applying that standard, and assessing the information that results from its application, feeds into and informs the IASB's review.
	Develop European Input to the IASB's post-implementation review of IFRS 8 'Operating Segments'*	Segment reporting is another major standard which the IASB has indicated it will conduct a post implementation review on. Disaggregated segment information is often cited by users to be a key aspect of the financial report that they rely on for decision-making. Again it will be important to capture the European experience in both applying the standard and in assessing the usefulness of information for users.
	Post-implementation review of IFRIC 12 'Service Concession Arrangements'*	IFRIC 12 has, according to some, pushed the accounting model to its limits and raised issues about accounting for long-term service concessions that involve the complex assignment of rights and obligations. Given the significance of IFRIC in setting out a framework for the financial reporting of such arrangements it would be useful to undertake a post-implementation review to understand how the standard has implemented in Europe and the reactions of users to the information reporting about such arrangement in the financial statements.
	Government grants	The IASB has had on its research agenda for sometime the development of work to replace IAS 20 'Accounting for Government Grants and Disclosure of Government Assistance'. It is not clear whether the standard complies with the Conceptual Framework and it contains too many options which potentially impair comparability. Now that the IASB has developed its revenue recognition model for exchange-based transaction it

\* This project would ideally build on the principles established in the policy project above but may be undertaken even if EFRAG has not developed in a separate project the European perspective on the policy (and methodology) to be applied to post-implementation reviews.

Rank	Project	Description
		would be appropriate to continue to develop that model to cover non-exchange transactions.
	Understanding the Decision Environments of Users of the financial report	The information needs of users are central to the objective of financial reporting. However, there is lack of intelligence about how users use information in the financial report to make decisions and assess the stewardship of resources. Users are often treated as a single group without adequate understanding of how they engage with financial information. In this context, our principal focus is on investors and analysts that support those making investment decisions. This project would attempt to discern from a practical study of European users how they decide what information is useful and how they use it in forming judgements about the performance, financial position and future cash generating ability of an entity.
	Application of IFRS to individual financial statements	IFRS currently do not distinguish the potential differences in user needs for individual and consolidated financial statements. Whilst there are strong accountability and stewardship reasons for preparing individual financial statements, it is not clear that IFRS are particularly well adapted to satisfying the needs of users at this level of reporting. This project would attempt to investigate the needs of users for individual financial statements and whether IFRS satisfy those needs and explore the possibility of different reporting models.
	Performance Reporting – Phase 3	<p>Performance reporting remains an aspect of financial reporting that is controversial and for which there still lacks clearly articulated principles to drive the presentation and display of information. This project has two key parts:</p> <ul style="list-style-type: none"> <li>• Establishing the principles that should drive the geography within the performance statement. In particular, identifying what should be included or excluded from net income (profit or loss).</li> <li>• Determining whether there is a basis for recycling and the circumstances under which it provides useful information to users of the financial statements.</li> </ul>
	Share-based payments	A number of commentators have suggested that IFRS 2 ‘Share-based Payment’ is difficult to understand and apply. Whilst work is being done to clarify the application of the standard, there is a growing consensus that the standard requires a fundamental review. This project would explore aspects of share-based payments from first principles.